Order Code RS20871
Updated October 12, 2007

CRS Report for Congress

The Iran Sanctions Act (ISA)

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Summary

No firms have been sanctioned under the Iran Sanctions Act (ISA). Set to expire in August 2006, legislation in the 109th Congress (the "Iran Freedom Support Act, P.L. 109-293) extended it until December 31, 2011, terminated application to Libya, and added provisions, although with substantial Administration flexibility in implementation. Proposed ISA-related legislation in the 110th Congress, such as H.R. 1400, which passed the House on September 25, 2007, would remove some of that flexibility. See also CRS Report RL32048, *Iran: U.S. Concerns and Policy Responses*, by Kenneth Katzman.

Background and Original Passage

The Iran Sanctions Act (ISA), originally called the Iran-Libya Sanctions Act (ILSA), was introduced during a tightening of U.S. sanctions on Iran during the Clinton Administration. In response to Iran's stepped up nuclear program and its support to terrorist organizations such as Hizbollah, Hamas, and Palestine Islamic Jihad, President Clinton issued Executive Order 12959 (May 6, 1995), banning U.S. trade with and investment in Iran. The rationale was that these sanctions would curb the strategic threat from Iran by hindering its ability to modernize its key petroleum sector, which generates about 20% of Iran's GDP. Iran's onshore oil fields, as well as its oil industry infrastructure, are aging and need substantial investment, and its large natural gas resources (940 trillion cubic feet, exceeded only by Russia) were un-developed when ISA was first considered.

U.S. allies refused to join the U.S. sanction, and the Clinton Administration and Congress believed that it might be necessary for the United States to try to deter their investment in Iran. The opportunity to do so came in November 1995, when Iran first opened its energy sector to foreign investment. To accommodate Iran's philosophy to retain control of its national resources, Iran developed a "buy-back" investment program in which foreign firms recoup their investments from the proceeds of oil and gas discoveries but do not receive equity stakes.

Report Documentation Page

Form Approved
OMB No. 0704-0188

1. REPORT DATE **12 OCT 2007**	2. REPORT TYPE	3. DATES COVERED **00-00-2007 to 00-00-2007**
4. TITLE AND SUBTITLE **The Iran Sanctions Act (ISA)**		5a. CONTRACT NUMBER 5b. GRANT NUMBER 5c. PROGRAM ELEMENT NUMBER
6. AUTHOR(S)		5d. PROJECT NUMBER 5e. TASK NUMBER 5f. WORK UNIT NUMBER
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) **Congressional Research Service, The Library of Congress,101 Independence Ave, SE,Washington,DC,20540-7050**		8. PERFORMING ORGANIZATION REPORT NUMBER
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)		10. SPONSOR/MONITOR'S ACRONYM(S) 11. SPONSOR/MONITOR'S REPORT NUMBER(S)

12. DISTRIBUTION/AVAILABILITY STATEMENT
Approved for public release; distribution unlimited

13. SUPPLEMENTARY NOTES

14. ABSTRACT

15. SUBJECT TERMS

16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT	18. NUMBER OF PAGES	19a. NAME OF RESPONSIBLE PERSON
a. REPORT **unclassified**	b. ABSTRACT **unclassified**	c. THIS PAGE **unclassified**	**Same as Report (SAR)**	**6**	

Standard Form 298 (Rev. 8-98)
Prescribed by ANSI Std Z39-18

Some in Congress, with input from the Clinton Administration, developed legislation to sanction such investment. On September 8, 1995, Senator Alfonse D'Amato introduced the "Iran Foreign Oil Sanctions Act" to sanction foreign firms' exports to Iran of energy technology. The bill passed the Senate on December 18, 1995 (voice vote) but, acknowledging the difficulty of monitoring all trade with Iran, sanctioned foreign *investment* in Iran's energy sector. On December 20, 1995, the Senate passed a version applying the legislation to Libya as well, which was refusing to yield for trial the two Libyan intelligence agents suspected in the December 21, 1988, bombing of Pan Am 103. The House passed its version of the bill, H.R. 3107, on June 19, 1996 (415-0), and then concurred on a slightly different Senate version adopted on July 16, 1996 (unanimous consent). It was signed on August 5, 1996 (P.L. 104-172).

Key Provisions. ISA requires the President to impose at least two out of a menu of seven sanctions on foreign companies (entities, persons) that make an "investment" of more than $20 million in one year in Iran's energy sector.[1] The sanctions menu (Section 6) includes (1) denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports to the sanctioned entity; (2) denial of licenses for the U.S. export of military or militarily-useful technology to the entity; (3) denial of U.S. bank loans exceeding $10 million in one year to the entity; (4) if the entity is a financial institution, a prohibition on its service as a primary dealer in U.S. government bonds; and/or a prohibition on its serving as a repository for U.S. government funds (each counts as one sanction); (5) prohibition on U.S. government procurement from the entity; and (6) restriction on imports from the entity, in accordance with the International Emergency Economic Powers Act (IEEPA, 50 U.S.C. 1701). In the original law, the President may waive the sanctions on Iran if the parent country of the violating firm agrees to impose economic sanctions on Iran (Section 4(c)) or if he certifies that doing so is important to the U.S. national interest (Section 9(c)). It terminates application to Iran if Iran ceases its efforts to acquire WMD and is removed from the U.S. list of state sponsors of terrorism. Its application to Libya terminated when the President determined on April 23, 2004, that Libya had fulfilled the requirements of all U.N. resolutions on Pan Am 103.

Traditionally skeptical of imposing economic sanctions, European Union states opposed ISA as an extraterritorial application of U.S. law and threatened counter-action in the World Trade Organization (WTO). In April 1997, the United States and the EU agreed to avoid a trade confrontation over it (and a separate "Helms-Burton" Cuba sanctions law, P.L. 104-114). This agreement contributed to a May 18, 1998, decision by the Clinton Administration to waive ILSA sanctions ("national interest" grounds — Section 9(c)) on the first project determined to be in violation: a $2 billion[2] contract, signed in September 1997, for Total SA of France and its partners, Gazprom of Russia and Petronas of Malaysia to develop phases 2 and 3 of the 25-phase South Pars gas field. In exchange, the EU pledged to increase cooperation with the United States on non-

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[1] For Libya, the threshold was $40 million, and sanctionable activity included exportation to Libya of a broad range of technology of which the export to Libya was banned by Pan Am 103-related Security Council Resolutions 748 (March 31, 1992) and 883 (November 11, 1993).

[2] Dollar figures for energy investment contracts with Iran represent public estimates of the amounts investing firms are expected to spend during the life of the project, which might in some cases be several decades.

proliferation and counter-terrorism, and the Administration indicated that EU firms would likely receive waivers for future similar investments in Iran.

ISA was to sunset on August 5, 2001, in the context of somewhat improved U.S. relations with both Iran and Libya. During 1999 and 2000, the Clinton Administration had eased the trade ban on Iran somewhat to try to engage the relatively moderate Iranian President Mohammad Khatemi. In 1999, Libya yielded for trial the Pan Am 103 suspects. However, proponents of renewal maintained that both countries would view its expiration as a concession. Renewal legislation was enacted in the 107th Congress (P.L. 107-24, August 3, 2001); it changed the definition of investment to treat any additions to pre-existing investment as new investment, and required an Administration report on ISA's effectiveness within 24 to 30 months of enactment. That report was submitted to Congress in January 2004 and did not recommend that ISA be repealed.

Modifications in the 109th Congress. During the 109th Congress, with U.S. concern about Iran's nuclear program increasing, ISA was again to sunset on August 5, 2006. Some Members, concerned that foreign companies had begun to openly ignore ISA, introduced the "Iran Freedom and Support Act" (H.R. 282, S. 333) to extend ISA indefinitely, to close some of its perceived loopholes, and to authorize funding for pro-democracy activities in Iran. These bills increased the requirements on the Administration to justify waiving sanctions on violators and, most notably, would have set a 90-day time limit for the Administration to determine whether an investment constitutes a violation of ISA (there is no time limit in the original law). H.R. 282 also would have cut U.S. foreign assistance to countries whose companies have violated ISA and applied the U.S. trade ban on Iran to foreign subsidiaries of U.S. companies. H.R. 282 was passed by the House on April 26, 397-21. To prevent ISA expiration while these bills were being considered, there was a temporary extension until September 29, 2006 (P.L. 109-267, signed August 4, 2006).

Toward the end of the 109th Congress, H.R. 6198, a modified version of H.R. 282, was introduced to address Administration concerns that H.R. 282 and S. 333 did not allow sufficient Administration flexibility. As did H.R. 282, it made sanctionable sales of WMD-useful technology or "destabilizing numbers and types of" advanced conventional weapons, and added a required determination that Iran "poses no significant threat" in order to terminate application to Iran. Unlike H.R. 282, it recommended, but did not require, a 180-day time limit for a determination of violation and changed the multi-lateral sanctions waiver provision ("4(c) waiver," see above) to a national security interest waiver. The law also recommended against U.S. nuclear agreements with countries that have supplied nuclear technology to Iran, extended ISA until December 31, 2011, dropped Libya from ISA, and contained a provision to try to prevent money-laundering by criminal groups, terrorists, or proliferators. It was passed by the House and Senate by voice vote and unanimous consent, respectively, and was signed on September 30, 2006 (P.L. 109-293). It changed the name of ILSA to the Iran Sanctions Act (ISA).

Effectiveness and Ongoing Challenges

Some believe ISA slowed Iran's energy development initially, but, as shown by the projects agreed to below, its deterrent effect appeared to weaken as foreign companies began to perceive that sanctions could be avoided. The projects listed in the table, all drawn from mainstream press reports, are said to be under review for ISA sanctions by

the State Department (Bureau of Economic Affairs), but no determinations of violation have been announced. State Department reports to Congress on ISA, required every six months, state that U.S. diplomats raise U.S. policy concerns about Iran with both investing companies and their parent countries. Most of the projects agreed before 2004 are now producing gas or oil. On the other hand, some experts believe that investment would have been much more extensive if not for both ISA as well as Iran's aggressive negotiating style. The investment has not boosted Iran's sustainable oil production significantly — it is still about 4 million barrels per day (mbd)[3] — and an analysis published by the National Academy of Sciences says that Iranian oil exports are declining to the point where Iran might have negligible exports of oil by 2015.[4] Others maintain that Iran's gas sector, virtually non-existent in 1998, is becoming an increasingly important factor in Iran's energy future because of foreign investment.

ISA's definition of "investment" does not specifically include oil or gas purchases from Iran. The Clinton and Bush Administration position has been that the construction of energy routes to or through Iran would constitute sanctionable activity because, as stated in the ISA definition of "investment" (Section 14), such routes would develop Iran's petroleum resources. The Clinton Administration used that argument to deter energy routes involving Iran and thereby successfully promote an alternate route from Azerbaijan (Baku) to Turkey (Ceyhan); this route became operational in 2005. However, neither Administration imposed sanctions on another project viewed as beneficial to U.S. ally Turkey: a natural gas pipeline from Iran to Turkey (each country constructing the pipeline on its side of their border). In July 1997, the State Department said that the project did not violate ISA because Turkey would be importing gas from Turkmenistan, not Iran, and would therefore not benefit Iran's energy sector directly. However, direct Iranian gas exports to Turkey began in 2001, in apparent contravention of Turkey's pledges and, as shown in the table, in July 2007 a preliminary agreement between Iran and Turkey would expand that arrangement to transshipment of Iranian gas to Europe, via the Iran-Turkey pipeline. It is not clear whether or not Iranian investments in energy projects in other countries, such as reputed Iranian investment to help build five oil refineries in Asia (China, Indonesia, Malaysia, and Singapore) and in Syria, reported in June 2007, would constitute sanctionable investment under ISA.

Further tests are looming, and some of the large, long-term (preliminary) deals between Iran and Indian, Chinese, and Malaysian firms, listed below, have the potential to significantly enhance Iran's energy export prospects. Most of the value of these agreements includes long-term contracts to purchase Iranian oil and gas, and the exact investment amounts for the exploration and production phases of these projects are not known. A related deal, particularly those involving Indian firms,[5] is the construction of

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[3] Testimony of Deputy Assistant Secretary of State Anna Borg before the House International Relations Committee, Subcommittee on the Middle East and Central Asia. June 17, 2003.

[4] Stern, Roger. "The Iranian Petroleum Crisis and United States National Security," *Proceedings of the National Academy of Sciences of the United States of America*. December 26, 2006.

[5] Some of the Indian companies that reportedly might take part in the pipeline project are ONGC Corp.; GAIL Ltd.; Indian Oil Corp.; and Bharat Petroleum Corp. Some large European companies have also expressed interest. See Solomon, Jay and Neil King. "U.S. Tries to Balance Encouraging India-Pakistan Rapprochement With Isolating Tehran." *Wall Street*

(continued...)

a gas pipeline from Iran to India, through Pakistan, with a possible extension to China. All three governments have appeared committed to the $4 billion to $7 billion project, which was planned to begin construction in 2007 and to be completed by 2010. However, press reports say India has not attended two recent meetings on the project, possibly suggesting its interest is waning. The three countries have not reached firm agreement on all the various issues, including a pricing formula, pipeline routing, transportation tariffs, pipeline security, and the Indian and Pakistani split of the gas supplies. U.S. officials, including Secretary of State Rice, have on several occasions "expressed U.S. concern" about the pipeline deal or have called it "unacceptable," but no U.S. official has stated outright that it would be sanctioned.

ISA is not the only mechanism available to the United States to try to limit investment in Iran. U.S. officials are having some success persuading European governments to limit new export credits guarantees to Iran, and to persuade European banks not to provide letters of credit for exports to Iran or to process dollar transactions for Iranian banks. This result is due not only to U.S. diplomacy but also to U.S. presentations of the financial risk posed by providing credit to Iran. The latest success of the policy came with an announcement in July 2007 by Deutsche Bank that it would seek no new business with Iran. The restrictions on financing are, according to Iranian and outside observers, making it more difficult to fund energy industry and other projects in Iran.

Proposed Further Amendments

In the 110th Congress, H.R. 1400 contains numerous provisions, some of which pertain to ISA, others of which do not. The bill passed the House on September 25, 2007 by a vote of 397-16. Among ISA-related provisions, H.R. 1400 would remove the Administration's ability to waive application of sanctions under ISA under Section 9(c), national interest grounds. However, the bill would not impose on the Administration a time limit to determine whether a project is sanctionable. Both it and other bills, its Senate counterpart S. 970, and another House bill, H.R. 957 (the latter passed the House on July 31, 2007) would expand the definitions of sanctionable entities to official credit guarantee agencies, such as France's COFACE and Germany's Hermes, and apply ISA sanctions to investment to develop a liquified natural gas (LNG) sector in Iran, which currently has no LNG export terminals. H.R. 1400 also would require the President to impose the ban on U.S. procurement from any entity sanctioned under ISA, and impose one other of the menu of sanctions. (For all the major provisions of H.R. 1400, see CRS Report RL32048, *Iran: U.S. Concerns and Policy Responses*.)

Another bill, H.R. 1357, would require government pension funds to divest of shares in firms that have made ISA-sanctionable investments in Iran's energy sector, and call on private pension funds to divest as well. Another bill, H.R. 2347, which passed the House on July 31, 2007, would protect from shareholder lawsuits fund managers that divest from firms that have made ISA-sanctionable investments. H.R. 2880 would apply ISA sanctions to sales to Iran of refined petroleum resources after December 31, 2007. The

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[5] (...continued)
Journal, June 24, 2005, p. A4.

U.N. Security Council — or a coalition of countries acting outside the Council — is said to be considering a worldwide ban on gasoline sales to Iran.

Post-1999 Foreign Investment in Iran's Energy Sector

Date	Field	Company(ies)	Value	Output Goal
Feb. 1999	Doroud (oil)	Totalfina Elf (France)/ENI (Italy)	$1 billion	205,000 bpd
Apr. 1999	Balal (oil)	Totalfina Elf/ Bow Valley (Canada)/ENI	$300 million	40,000 bpd
Nov. 1999	Soroush and Nowruz (oil)	Royal Dutch Shell	$800 million	190,000 bpd
Apr. 2000	Anaran (oil)	Norsk Hydro (Norway)		?
July 2000	Phase 4 and 5, South Pars (gas)	ENI	$1.9 billion	2 billion cu.ft./day
Mar. 2001	Caspian Sea oil exploration	GVA Consultants (Sweden)	$225 million	?
June 2001	Darkhovin (oil)	ENI	$1 billion	160,000 bpd
May 2002	Masjid-e-Soleyman (oil)	Sheer Energy (Canada)	$80 million	25,000 bpd
Sep. 2002	Phase 9 and 10, South Pars (gas)	LG (South Korea)	$1.6 billion	?
Oct. 2002	Phase 6, 7, 8, South Pars (gas)	Statoil (Norway)	$2.65 billion	3 billion cu.ft./day
Feb. 2004	Azadegan (oil)	Inpex (Japan) 10% stake	$200 million Japan stake	260,000 bpd
Oct. 2004	Yadavaran (oil); deal includes gas purchases for 30 years	Sinopec (China) and ONGC (India)	$70 billion (value of exploration not known)	300,000 bpd
June 2006	Gamsar block (oil)	Sinopec (China)	$50 million	?
Totals			**$80 billion+**	**Oil: 1.2 million bpd Gas: 5 billion cu.ft/day+**
Pending Deals/Preliminary Agreements				
Golshan and Ferdows (offshore gas, includes downstream development)		SKS Ventures (Malaysia)	$20 billion	100 million cu.ft/day
North Pars Gas Field (offshore gas)		China National Offshore Oil Co.	$16 billion (includes gas purchases	3.6 billion cu.ft/day
Phase 13 and 14 - South Pars (gas); includes building a liquified natural gas (LNG) terminal		Royal Dutch Shell and Repsol (Spain)	$10 billion	?
Phase 22, 23, 24 - South Pars (gas), plus agreement to transport Iranian gas to Europe (signed July 13, 2007)		Turkish Petroleum Company (TPAO)	$3 - $4 billion	2 billion cu. ft/day
Construction of a petrochemicals plant in Iran, near South Pars gas field. Might produce rubber, plastics, other petroleum-derived products. (Announced Sept. 2007)		GAIL-India, Jaipan Industries Ltd. (India)	$2.3 billion	